

# ANALYSIS OF AMENDED BILL

## Franchise Tax Board

Author: Dutton Analyst: Rachel Coco Bill Number: AB 2859  
Related Bills: See Legislative History Telephone: 845-4328 Amended Date: March 30, 2004  
Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Employer Contributions To Unemployment Fund Credit/Employment Of Veteran Or Individual Separated From Armed Services Or National Guard

### SUMMARY

This bill would provide employers a tax credit equal to the amount paid into the Unemployment Fund.

### SUMMARY OF AMENDMENTS

The March 30, 2004, amendments removed language that would have made changes to the Unemployment Insurance Law.

The March 30, 2004, amendments added language that would provide a tax credit for taxpayers that employ recently separated members of the armed services or the California National Guard or veterans who participate in an employment training program.

This is the department's first analysis of the bill.

### PURPOSE OF THE BILL

According to the author's office, the purpose of the bill is to encourage industry to recruit service people into the workforce.

### EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective and operative for taxable years beginning on or after January 1, 2004.

### POSITION

Pending.

### ANALYSIS

#### FEDERAL/STATE LAW

Existing state and federal laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption) or to influence behavior, including business practices and decisions (e.g., research credits or economic development area hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

#### Board Position:

<input type="checkbox"/> S	<input type="checkbox"/> NA	<input type="checkbox"/> NP
<input type="checkbox"/> SA	<input type="checkbox"/> O	<input type="checkbox"/> NAR
<input type="checkbox"/> N	<input type="checkbox"/> OUA	<input checked="" type="checkbox"/> PENDING

#### Department Director

#### Date

Gerald H. Goldberg

4/30/04

Existing state and federal laws also allow a taxpayer to deduct expenses paid or incurred in the ordinary course of a taxpayer's business, including employee wages and benefits.

The State Treasurer's office maintains the Unemployment Fund for purposes of providing weekly unemployment insurance payments to workers who lose their job through no fault of their own. The Unemployment Fund is financed through unemployment taxes paid by employers. The tax is required on up to \$7,000 in wages paid to each employee. The actual tax rate varies for each employer, depending in part on the amount of unemployment benefits paid to former employees. Thus, an employer would have a lower tax rate if former employees made fewer claims on the employer's account.

Under current federal law, the Uniformed Services Employment and Reemployment Rights Act of 1994 (Public Law 103-353) requires employers to re-hire reservists and Guardsmen who have been called to federal active duty for periods less than five years.

### THIS BILL

This bill would provide a tax credit in an amount equal to the amount paid into the Unemployment Fund by a qualified taxpayer. The bill states that the credit would be allowed based on the amount paid into the fund during the first year of employment of any qualified employee.

The bill defines "qualified employee" as 1) an individual who is separated from the armed services or the California National Guard and is hired by a qualified taxpayer within six months of separation, or 2) a veteran who has either completed within six months of being hired or is a participant in an employment training or development program.

The bill defines "qualified taxpayer" as a taxpayer that makes employer contributions to the Unemployment Fund and employs one or more qualified employees.

This bill would allow any unused credit to be carried over until exhausted.

### IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

The bill provides that a qualified employee is an individual who is separated from the armed services or the California National Guard or a veteran who has or is participating in a training program. However, the bill lacks language that would require documentation for purposes of certifying the eligibility of an employee. The author may wish to amend the bill to require the employer to obtain documents verifying the employee's eligibility.

The bill uses the phrase "separated from the armed services of the United States or the California National Guard" to define a qualified employee. It is unclear what would qualify as "separation." The author may wish to amend the bill to provide circumstances or requirements necessary to qualify an eligible employee, such as "separated from active duty,"

The bill specifies that a qualified taxpayer is one that makes “employer” contributions to the Unemployment Fund. However, in some instances employers deduct the amount of the contribution to the fund from employee wages. It is unclear whether a taxpayer that uses employee wages as contribution to the fund would qualify for this credit.

The bill uses terms that are undefined by the Revenue and Taxation Code (R&TC). The author may wish to amend the bill to define the terms “California National Guard” and “veteran” in order to avoid confusion between taxpayers and the department.

#### TECHNICAL CONSIDERATIONS

The provision defining “qualified employee” contains unnecessary language. If the author intends only one of the conditions to be satisfied, then “or both” should be removed. If the intent is to require that both conditions be satisfied, then “either or” should be removed.

The bill uses the term “armed services of the US,” which is undefined. The author may wish to amend the language to refer to the “armed forces of the US,” which is defined within the R&TC.

#### **OTHER STATES’ INFORMATION**

*Illinois, Massachusetts, Michigan, Minnesota, and New York* tax laws do not provide a credit comparable to the credit that would be allowed by this bill. The laws of these states were reviewed because their tax laws are similar to California’s income tax laws.

#### **FISCAL IMPACT**

This bill would not significantly impact the department’s costs.

#### **ECONOMIC IMPACT**

##### Revenue Estimate

This bill would result in the following revenue losses:

Revenue Impact of AB 2859 (Assumes enactment after 6/30/04) (\$ Millions)			
Fiscal Year	2004-05	2005-06	2006-07
Revenue Loss	-\$2.5	-\$2.5	-\$2.5

This estimate does not take into account any possible changes in employment, personal income, or gross state product that might result from this bill.

### Revenue Discussion

There are approximately 170,000 regular military personnel stationed in California and approximately 24,000 reserves on active duty in the California National Guard.

Based on a National Guard survey reported in the *USA Today* in 2003 about 16% of individuals leave the military as a result of retirement, injuries, or a decision not to re-enlist. For regular military personnel, assuming that one-third of those leaving the military do so as a result of not re-enlisting, then approximately 9,000 military personnel would be available for employment in California each year. If one-half found employment in California within six months, then 4,500 individuals would be generating unemployment insurance credits for their employers.

Of the 24,000 reserves on active duty, the majority have jobs to return to after their deployment. If 5% or 1,200 were unemployed at the time they were called up for duty or lost their former jobs and found employment after their tour, then an additional 1,200 individuals would potentially qualify their employers for the credit.

The unemployment tax rate is a maximum of 6.2% of the first \$7,000 of wages or \$434. It is estimated that 5,700 individuals could be employed resulting in a revenue loss of approximately \$2.5 million annually beginning in 2004-05. (4,500 military + 1,200 reserves x \$434 credit = \$2.5 million)

### **ARGUMENTS/POLICY CONCERNS**

This bill does not specify a repeal date or limit the number of years for the carryover period. Credits typically are enacted with a repeal date to allow the Legislature to review their effectiveness periodically. However, even if a repeal date were added, the department would be required to retain the credit on the tax forms indefinitely because an unlimited credit carryover period is allowed. Recent credits have been enacted with a carryover period limitation since experience shows credits are typically used within eight years of being earned.

This bill would have the effect of providing a double benefit for deductible benefits by virtue of this credit and the ordinary deduction of these payments from the income of the trade or business.

Currently, employers are required by federal law to re-hire service members once they have completed their tour of duty. Thus, this bill could be seen as providing an incentive for complying with existing law.

This bill lacks language requiring that qualified employees be employed and performing services within California. Without such language, the bill could be interpreted to provide the credit for employees working outside of California.

Credits generally are provided as a percentage of amounts paid or incurred. This bill would allow a 100% credit, which is unprecedented.

### **LEGISLATIVE STAFF CONTACT**

Rachel Coco  
Franchise Tax Board  
845-4328

Brian Putler  
Franchise Tax Board  
845-6333

[rachel.coco@ftb.ca.gov](mailto:rachel.coco@ftb.ca.gov)

[brian.putler@ftb.ca.gov](mailto:brian.putler@ftb.ca.gov)